

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeals of)
MYRON (MIKE) AND NORALEE JACOBSON)
and GEORGE AND GENEVIEVE STUDINGER)

Appearances:

For Appellants: Archibald M. Mull, Jr.,
Attorney at Law

For Respondent: A, Ben Jacobson,
Associate Tax Counsel

O P I N I O N

These appeals are made pursuant to section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on protests to proposed assessments of additional personal income tax against Myron (Mike) and Noralee Jacobson in the amounts of \$254.90, \$341.59, \$308.71 and \$245.62 for the years 1952, 1953, 1954 and 1955, respectively, and against George and Genevieve Studinger in the amounts of \$335.69, \$500.74, \$521.46 and \$375.46 for the years 1952, 1953, 1954 and 1955, respectively.

During the years under appeal, appellants Myron (Mike) Jacobson and George Studinger operated a partnership business in San Francisco known as the Yellow Cab Smoke Shop.

The Yellow Cab Smoke Shop sold tobacco products, liquor, candy and other similar items. Its customers were almost exclusively cab drivers for the Yellow Cab Company of San Francisco.

In the same location where merchandise was sold, the Smoke Shop conducted a dice game called "Selection," maintained about five pinball machines, most of which were multiple-odd bingo pinball machines, and operated a card room. Players who won at the dice game were allowed to select merchandise at the regular retail price in redemption of their winnings, as were players of the bingo pinball machines for unplayed free games which they won. The winnings of each player were customarily recorded in a "cuff" book which the Smoke Shop maintained. A winner could then select his merchandise whenever he wished. With respect to the card room, the Smoke Shop collected seat rentals from the players, who apparently played against each other rather than against the house,

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Respondent disallowed all expenses on the tax returns filed for the Yellow Cab Smoke Shop pursuant to section 17297 (17359 prior to June 6, 1955) of the Revenue and Taxation Code which reads:

In computing taxable income, no deductions shall be allowed to any taxpayer on any of his gross income derived from illegal activities as defined in Chapters 9, 10 or 10.5 of Title 9 of Part 1 of the Penal Code of California; nor shall any deductions be allowed to any taxpayer on any of his gross income derived from any other activities which tend to promote or to further, or are connected or associated with, such illegal activities.

In Appeal of Advance Automatic Sales Co., Cal. St. Bd. of Equal', Oct. 9, 1962, CCH Cal. Tax Rep. Par. 201-984, 2 P-H State & Local Tax Serv. Cal. Par. 13288, we held the ownership or possession of a pinball machine to be illegal under Penal Code sections 330b, 330.1 and 330.5 if the machine was predominantly a game of chance or if cash or other thing of value was paid to players for unplayed free games, and we also held bingo pinball machines to be predominantly games of chance.

Section 330 of the Penal Code makes it illegal to conduct any banking game played with dice for "money, checks, credit, or other representative of value, ..." **h banking game is one in which one person takes all that is lost by the bettors and pays out all that is won, as contrasted with a game in which the players bet against each other, (People v. Ambrose, 122 Cal, App. 2d Supp. 966(265 P.2d 191).)**

Since the Smoke Shop possessed bingo pinball machines and also gave merchandise to winning players of the pinball machines, and since the Smoke Shop conducted a banking game played with dice, giving credit for merchandise to the winners of that game, the pinball and dice game phases of the business were illegal. Respondent was therefore correct in applying section 17297.

While dice game payouts were recorded, there were no records of amounts paid to winning players on pinball machines, and respondent estimated these unrecorded amounts as equal to 50 percent of the total amounts deposited in the pinball machines. The basis for the 50 percent estimate was primarily the experience of respondent's auditor in auditing other pinball machine operators.

As we held in Appeal of C. B. Hall, Sr., Cal. St. Bd. of Equal', Dec. 29, 1958, 2 CCH Cal. Tax. Cas. Par. 201-197, 3 P-H State & Local Tax Serv. Cal. Par. 58145, respondent's computation of gross income is presumptively correct. There is no evidence which would indicate that the 50 percent payout estimate was excessive and, under the circumstances, it must be sustained.

Records of the Yellow Cab Smoke Shop did not segregate the bingo pinball

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income from the flipper pinball income and respondent has made no attempt at such a division. It is first necessary to determine the portion of the recorded income which was derived from bingo pinball machines in order to compute the unrecorded amount of payouts on such machines. At the hearing of this matter, appellant Myron (Mike) Jacobson testified that the partnership had more bingo pinball machines than flipper pinball machines. On the basis of this testimony and our understanding that bingo pinball machines produce a much greater return than flipper pinball machines, we conclude that 90 percent of the recorded income from pinball machines was attributable to bingo pinball machines*

Tax returns filed by the partnership indicate that the illegal activities contributed in excess of 50 percent of the reported gross profit of the Yellow Cab Smoke Shop during each of the years under appeal. It is clear that the merchandising and card room operation played secondary and complementary roles and were associated and connected with the illegal activities. Consequently, the expenses of the entire business were properly disallowed.

O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protests of Myron (Mike) and Noralee Jacobson to proposed assessments of additional personal income tax in the amounts of \$254.90, \$341.59, \$308.71 and \$245.62 for the years 1952, 1953, 1954 and 1955, respectively, and of George and Genevieve Studinger in the amounts of \$335.69, \$500.74, \$521.46 and \$375.46 for the years 1952, 1953, 1954 and 1955, respectively, be modified in that the gross income is to be recomputed in accordance with the opinion of the board. In all other respects the action of the Franchise Tax Board is sustained.

Done at **Sacramento**, California, this 7th day of May, 1963, by the State Board of Equalization.

<u>Paul R. Leake</u>	, Chairman
<u>Richard Nevins</u>	, Member
<u>Geo. R. Reilly</u>	, Member
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ATTEST: Dixwell L. Pierce, Secretary